Guidelines

CRUDE OIL ROYALTY HOLIDAY PROGRAM

EXPLORATORY GAS WELL INCENTIVE PROGRAM

DEEP GAS ROYALTY HOLIDAY PROGRAM

Alberta

ENERGY AND
NATURAL RESOURCES
Mineral Revenues

GUIDELINES

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PREFACE

On June 24, 1985, Premier Peter Lougheed and Energy and Natural Resources Minister John Zaozirny released a comprehensive statement on Alberta's Oil and Gas Incentives. Three new programs were introduced:

Crude Oil Royalty Holiday Program
Exploratory Gas Well Incentive Program
Deep Gas Royalty Holiday Program

This manual has been prepared for the convenience of those seeking to utilize the benefits offered by these programs. It will serve as a guide in understanding the legislation relating to these programs. The department would like to acknowledge the assistance and co-operation of the Canadian Petroleum Association and the Independent Petroleum Association of Canada in preparing these guidelines.

The information contained in the manual is of an administrative, procedural and explanatory nature. The applicable legislation as contained in Alberta Regulations 93/74 and 16/74 as amended, remains the final authority for these programs.

CONTENTS

Appendices

Crude Oil Royalty Holiday Program

Exploratory Gas Well Incentive Program

Deep Gas Holiday Program

List of Illustrations

Crude Oil Royalty Holiday Program Typical Qualifying Intervals

Exploratory Gas Well Incentive Program Typical Qualifying Intervals

Deep Gas Royalty Holiday Program Typical Qualifying Intervals

INTRODUCTION

In the spring of 1985, a thorough review of oil and gas industry incentives was conducted with the objective of maintaining a strong and active oil and gas industry in Alberta. Consistent with the positive thrust of the Energy Pricing and Taxation Understanding of March 28, 1985, this review concluded that certain changes were required to ensure that the gains resulting from the deregulation of crude oil pricing flow through to the industry, and that natural gas producers continue to be competitive in natural gas markets.

In response, the Government of Alberta has introduced major initiatives in the form of the Crude Oil Royalty Holiday Program, the Exploratory Gas Well Incentive Program and the Deep Gas Royalty Holiday Program.

The Crude Oil Royalty Holiday Program is intended to provide a reward to the successful explorer. This will be in the form of a royalty holiday applicable to wells drilled or deepened into new conventional oil pools or extensions of current pools, where the drilling was begun during the period June 1, 1985 to May 31, 1988, inclusive.

The Exploratory Gas Well Incentive Program is designed to provide continued support to gas exploration by providing a defined royalty holiday to production from successfully completed exploration wells. The program is in effect from August 1, 1985 to May 31, 1988, inclusive.

The Deep Gas Royalty Holiday Program is designed to reward the successful discovery and production of natural gas from deep gas pools. The program is in effect from June 1, 1985.

CRUDE OIL ROYALTY HOLIDAY PROGRAM

Eligibility

Requirements

A new well or the deepening of an existing well must meet two basic criteria to qualify for a crude oil royalty holiday.

Firstly, the spudding of the well, or the beginning of drilling to deepen an existing well must start after May 31, 1985 but before June 1, 1988.

Secondly, the drilling spacing unit (DSU) applicable to the zone in which the new or deepened well is completed must be wholly outside the pool boundaries, as defined by the Energy Resources Conservation Board (ERCB) in subsisting G-Orders at June 1, 1985.
The department is aware that wells drilled and completed prior to June 1, 1985 may be located in areas that have not been designated as pools by ERCB G-Orders. For the purposes of this program, where a well has produced prior to June 1, 1985 according to ERCB records and is located in such an area, then the pool boundary, with respect to that well, shall be defined as the DSU existing at June 1, 1985 or the 64 hectare DSU associated with the particular well, whichever is smaller.

Oil Sands Areas

This program is intended to provide incentives for successful drilling of wells in search of conventional oil pools. Accordingly, a well drilled within the boundaries and zones of an Oil Sands Area (OSA) Order issued by the ERCB is ineligible under this program. For the current status of all such orders see OSA 1 through 3 and ERCB Informational Letter 84-7 of August 7, 1984. The department, as part of the application approval process, will confirm that the completed well is not within the boundaries of an Oil Sands Area or zone. A well completed within an Oil Sands Area and zone may be deepened. Any such well, subject to all other eligibility requirements, may receive benefits under this program if completed in a zone not included in the applicable Oil Sands Area.

The Crown has entered into contracts with certain parties covering production and royalty requirements with respect to all wells within a defined area and completed into specified zones. Any well covered by such a contract is not eligible under this program.

Experimental Schemes

Experimental schemes currently have effective incentives. Consequently, any well spudded or deepened at a location already within an area covered by an ERCB experimental status approval is not eligible for this crude oil royalty holiday. If an area ceases, for any reason, to retain its experimental status, then this eligibility restriction is no longer in effect.

Enhanced Oil Recovery

Wells included in schemes approved for benefits under Section 4.2 of the Petroleum Royalty Regulations (A.R. 93/74, as amended) may not simultaneously receive a benefit under this program.

Each licensee of an eligible well who elects to receive benefits under the Crude Oil Royalty Holiday Program may not include the well's drilling and other costs in the costs reported for purposes of section 4.2 royalty relief.

It is the responsibility of the licensee to select either program, file an application for the Crude Oil Royalty Holiday if desired, and exclude the appropriate costs for the well from those reported under Section 4.2.

Off Target Wells

Under the Oil and Gas Conservation Regulations (A.R. 151/71) the ERCB has the authority to designate a well as being "off target". A well that is designated as being off target and on which a

penalty is levied is not eligible for the Crude Oil Royalty Holiday Program. The licensee may file an application with the ERCB for a spacing unit or target area change. If the application is approved and the well is no longer considered off target, the well may be fully eligible for the benefits under this program, subject to all other eligibility requirements. Any such benefits will be received from the month in which the application to the ERCB is approved, a royalty holiday application is received by the department, or production started, whichever is latest.

It is the responsibility of the licensee to inform the department as to the lifting of the off target designation. The department will recognize the ruling of the ERCB as final in all situations relating to off target wells.

Freehold

The Crude Oil Royalty Holiday Program applies only in situations where there is a Crown interest in production and is limited to the extent of that interest. Hence, wells on wholly freehold property are not eligible for any benefit under this program.

Prior Benefits

It is the intention of the department to prohibit a well from receiving benefits under more than one incentive program. Accordingly, a well that has already received a royalty exemption as an incentive exploratory well under the Exploratory Drilling Incentive System (EDIS) (A.R. 378/72) or any subsequent EDIS regulation, or a well receiving a benefit under the Oil Royalty Exemption System (ORES) (A.R. 139/84) will only be eligible for benefits under this program, in respect of a new qualifying interval.

DSU Limitation

In cases where a well in the DSU applicable to the zone in which the new or deepened well has been completed has at any time received a royalty exemption under EDIS (A.R. 378/72) or any subsequent EDIS Regulation, ORES or this program, then no subsequently drilled well in the same DSU can be eligible for this Crude Oil Royalty Holiday.

Licensees should note that a well in a DSU which has been the beneficiary of drilling credits, but not a royalty exemption, does not disqualify another well in the same DSU from receiving benefits under this program.

Qualifying Interval

New Well

One of the benefit criteria under this program is depth related. The term "qualifying interval" has been developed to cover the drilled well depth that is used to determine benefits. In the case of a newly drilled well, the qualifying interval is the drilled well depth (Figure 1) or the drilled depth to the base of the crude oil bearing interval of the deepest zone from which crude oil is being produced in paying quantities (Figure 2), whichever is shallower. The department, as a general rule, will assume that when an owner

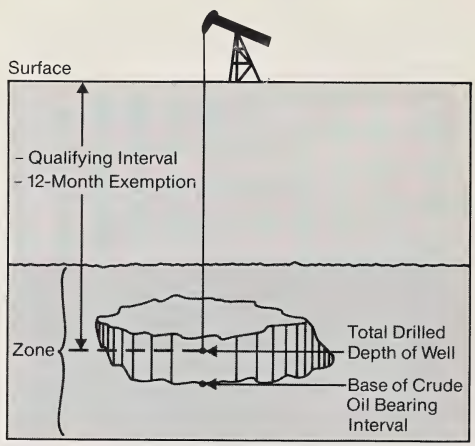


Figure 1 - New well qualifying interval where the completion point is at the total drilled depth.

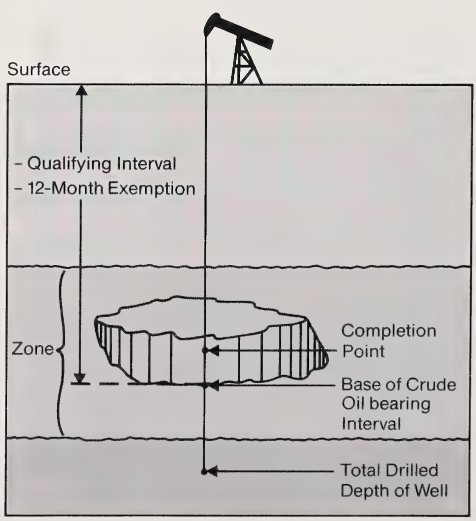


Figure 2 - New well qualifying interval where the completion point is not at the total drilled depth.

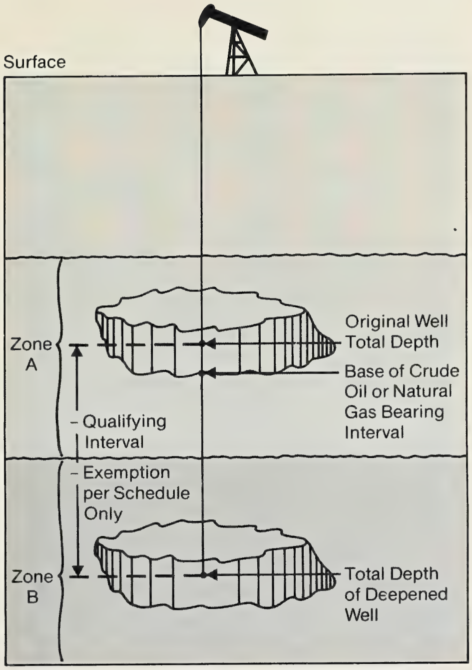


Figure 3 - Deepened well qualifying interval where the completion point is at the total drilled depth.

begins to sell production the well is producing crude oil in "paying quantities". In cases of doubt the department may conduct a specific review and make a final determination.

Deepened Well

For deepened wells, the qualifying interval is the drilled well depth from the previously drilled total depth of the well to the current drilled total depth (Figure 3 and 4), or the base of the crude oil bearing interval of the deepest zone from which crude oil is being produced in paying quantities (Figure 5), whichever is shallower. Of particular note is the fact that the qualifying interval may extend from the total depth of a previously drilled well that was in an interval that was natural gas bearing only.

A well may also be deepened from a zone in which there is no crude oil or natural gas. In these circumstances, the qualifying interval is measured from the total depth of the original well to the base of the crude oil bearing interval in the deepest zone from which the well is producing crude oil in paying quantities, or the deepened well's total depth, whichever is shallower.

As with a new well, the department will apply the same general rule for determining that there is

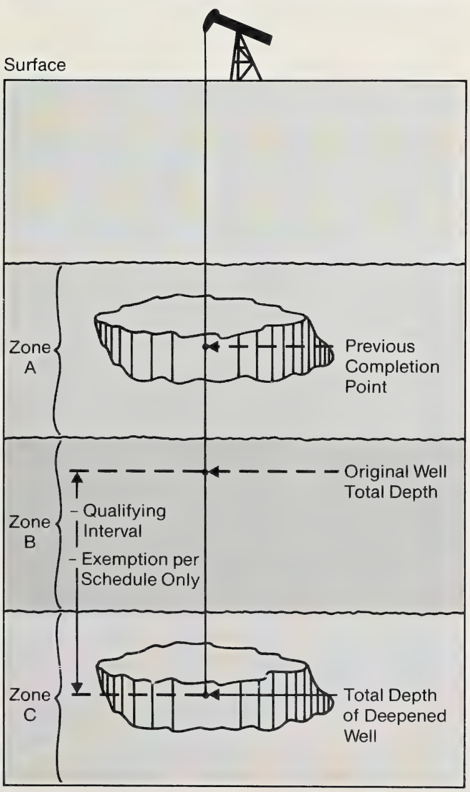


Figure 4 - Deepened well qualifying interval where the original well total depth is below the crude oil bearing interval in which the original well is completed.

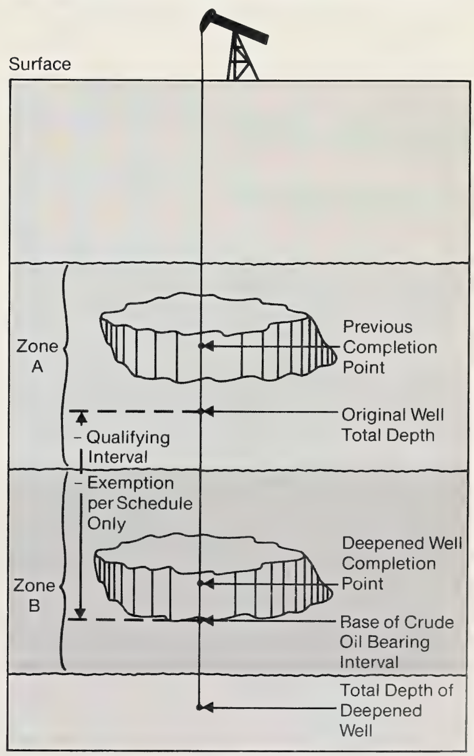


Figure 5 - Deepened well qualifying interval where the total depth of the deepened well exceeds the base of the crude oil bearing interval.

production in paying quantities. In cases of doubt the department may conduct a specific review and make a final determination.

Benefits

Application Procedure

Application must be made on the Crude Oil Royalty Holiday Program Application (Form No. 547) and sent directly to the Incentives Branch of the Mineral Revenues Division. Application forms can be obtained directly from the Mineral Revenues Division or from the locations noted on page ii. Incorrect applications will be returned. In these cases there may be a delay in the receipt of the benefits. This is particularly relevant where production has begun before a complete application is submitted. If an incomplete application is subsequently resubmitted and approved, then the date of the initial submission will be considered the effective month for the purpose of determining when the royalty holiday commences.

Applications must be received within six months of the finished drilling date for the well. In addition, the legislation requires that the drilling or deepening of the well be conducted diligently and continuously.

Delays caused by actions of a government department or agency may extend the time available for spudding or commencement of deepening.

Effective Date

The royalty holiday begins either on the first day of the month in which production begins or an application is received, whichever is later. This permits licensees to select the month of commencement of the royalty holiday. As desired, applications may be filed in order to exclude the month(s) in which test production occurs and/or to start the royalty holiday in the first month in which full production is expected.

Benefit Amount

The aggregate Crown royalty share volume to be exempted from royalty for a particular well is determined from the chart shown as Appendix 1 (Schedule D to the Petroleum Royalty Amendment Regulation, A.R. 216/85). To calculate the benefit amount for a well in a specific area, when the qualifying interval is measured from surface the cumulative value at the deepest drilled depth not exceeding the depth drilled is added to the incremental value at that point times the number of metres in excess of that depth.

When the qualifying interval is not measured from surface, i.e. it is in a deepened well, the benefit amount at both the beginning and finishing points of the qualifying interval must be computed in each case as if a well had been drilled from surface to each of those points. The difference between the two amounts so determined is the benefit for the deepened well.

The regulation stipulates that the well licensee is the party entitled to apply for the benefits under this program. Benefits may only be received by way of an offset against royalties that are payable on the well's production. As necessary, licensees may designate an agent, e.g. an operator, for the purposes of administering their interests under this program. It is not necessary to advise the department as to any agency arrangement.

It is the responsibility of well interest owners to obtain amendments to operating agreements, as required, to ensure receipt of an appropriate share of the benefits. The department will not and does not have the authority to settle benefits with any party other than the licensee or the agent of the licensee.

Limitations on Benefits

The royalty holiday for new wells will last until the volume of crude oil exempted equals the amount determined from the chart shown as Appendix 1, or until 12 calendar months (not necessarily consecutive) of royalty-free production have occurred, whichever is later.

Regardless of which of the two limitations is applicable, the value of the royalty holiday cannot exceed $1 million per well. To determine the volume of crude oil which is valued at $1 million for a particular well, the limit, i.e. $1 million, is divided by the par price in effect during either the month in which production begins or an application is received, whichever is later. The amount so determined will be fixed for the duration of the royalty exemption for the particular well and will not be affected by any subsequent changes in the par price.

In the case of deepening there is no 12-month time period exemption. The benefit computed from Appendix 1 will be received, subject only to the $1 million limit.

Benefit entitlements earned under this program must be used on or before May 31, 1993. Also, any unused benefits at the time of a well abandonment are lost. Production should be planned accordingly as the department does not have any discretionary authority to vary these conditions.

Crown/Freehold

Many production entities are split between the Crown and Freehold interests. In these situations, it is the intent of the program to provide a benefit with respect to the Crown's interest in production only. Accordingly, once the benefit is determined as if it were a 100% Crown well, it must be reduced to the level of the Crown interest.
This also applies to the overall limitation of $1 million per well; i.e. the cap is reduced to $1 million times the Crown interest in the production entity. The 12-month time period exemption remains unaffected.

The Crown interest in production will be as of the date of application or first production, whichever is later, and will be on the basis of the Crown/ Freehold production split of the production entity in the month preceding the first month in which the royalty holiday applies.

Once the maximum level of the benefit to a Crown/ Freehold well has been set, it will not be varied regardless of any subsequent changes in the Crown interest in the production entity.
As the benefit can only be received by way of an offset against royalties that are payable on the well's production, where the Crown's interest falls to zero per cent the unexpired benefit would become unusable and would be effectively lost, unless a restructured production entity restores a Crown interest to the well prior to May 31, 1993.

Twin Wells

The department recognizes that in certain circumstances a well may be inadvertently damaged, resulting in the need to drill a twin well. The department will rely on the recommendation of the ERCB as to the necessity for the well.

The unexpired benefits of the royalty holiday at the time the originally approved well was damaged and ceased production may be transferred to the twin well. To be eligible the twin well must be:

a) spudded after May 31, 1985;
b) located in the same DSU or legal subdivision, whichever is of lesser area, as the well being twinned; and,
c) capable of producing crude oil which, in the opinion of the ERCB, is not recoverable from the original well due to its inadvertent damage.

It is the responsibility of the licensee to advise the department of the new well identifier at the earliest opportunity. No increase or extension of a royalty holiday benefit will be gained by the drilling of a twin well.

Drilling Areas

The level of benefits available varies depending upon the area of the province in which drilling occurs. For this purpose, the province has been divided into four areas: the Northern, Foothills, Plains and Central Areas. Benefits under the Northern and Foothills areas are the same.
Each area is specifically defined by reference to township and range in Schedule E to the Petroleum Royalty Amendment Regulation (A.R. 216/85).

Applicants should confirm the location of their well and hence benefit eligibility when applying. In the event of a disagreement on benefit entitlement due to location, the areas as defined in Schedule E (A.R. 216/85) will be used by the department to reach a final decision.

Appeals

An applicant may appeal each denied application in writing to the Associate Deputy Minister within 90 days of the date of the notice of the decision. Additional information must be presented in the appeal statement to justify a review of the department's decision.

The department will expeditiously review the appeal and advise the applicant as to the result. If the appeal is granted and the application approved, the benefit will be applied from the month in which the original application was made or the month in which production commenced, whichever is later.

Oil Royalty Exemption System (ORES)

The ORES program ended July 31, 1985.
An operator has up to six months after the finished drilling date of a well to place an application with the department, provided that spudding or commencement of deepening began on or before July 31, 1985. The previously published eligibility requirements and administrative guidelines remained in effect for the ORES program until that date. In cases where an operator, due to the actions of a government department or agency, has incurred a delay such that the deadline cannot be met, the department should be informed of the circumstances upon application. Reasonable requests for extensions will be considered.

During the transition period, i.e. June 1 - July 31, 1985, the licensee of an eligible well may

obtain benefits under either ORES or the new Crude Oil Royalty Holiday Program. It is the licensee's sole responsibility to decide which benefit is desired and apply accordingly. The department does not have the authority to permit switching between programs.

Exploratory Drilling Incentive System (EDIS)

The Exploratory Drilling Incentive System ended July 31, 1985. The previously published eligibility requirements and administrative guidelines remained in effect until that date. In cases where an operator has incurred a delay due to the actions of a government department or agency such that the deadline cannot be met, the department should be informed of the circumstances upon application. Reasonable requests for extensions will be considered.

During the transition period, i.e. June 1 - July 31, 1985, the operator of an eligible well may obtain benefits under EDIS or, if necessary by agreement with the licensee, under ORES or the new Crude Oil Royalty Holiday Program. It is the sole responsibility of the operator and licensee to decide which benefit is desired and apply accordingly. The department does not have the authority to permit switching between programs.

Certain benefits, in the form of credits to the account of the beneficiary of a crude oil royalty exemption, may have been earned as of July 31, 1985. It is the intent of the department to provide a reasonable time for the use of these benefits. To meet this objective, a period to December 31, 1990 is being allowed to make use of these earned benefits. Any unused amounts outstanding at that date will be lost. Owners of the benefits are urged to plan their affairs to meet this date as the enabling legislation does not give the department any discretionary authority with respect to extension of the deadline.

EXPLORATORY GAS WELL INCENTIVE PROGRAM

Eligibility

Requirements

To be eligible a well must be certified by the Energy Resources Conservation Board (ERCB) as an exploratory gas well and the spudding of the well, or the beginning of drilling to deepen an existing well must start after July 31, 1985 and before June 1, 1988.

The department will, in all instances, accept the determination of the ERCB as to whether or not a well is certifiable as an exploratory gas well.

Exempt Production

The production from an eligible well must meet certain requirements to qualify for royalty exemption. Specifically, the production must be from a natural gas bearing interval within the qualifying interval of the well and from a depth in excess of 600 metres, and the production obtained must be attributable to the drilling spacing unit (DSU) applicable to the zone in which the new or deepened well is completed.

Cases where the pool straddles the boundary between a non-qualifying interval and a qualifying interval or straddles the 600-metre limit will be reviewed on an individual basis by the department. They will generally qualify if production in paying quantities initially occurs in the portion of the pool and qualifying interval which is below 600 metres.

Drilling credits earned under EDIS by a well within 4.8 kilometres of an eligible well will not disqualify the eligible well from receiving benefits under this program.

ERCB Certification

The ERCB will certify a well to be drilled or deepened for gas that satisfies the necessary conditions at the time of licensing or certificate renewal. A copy of the initial certificate is attached to the well licence, and a copy of the "new" (renewed) certificate, if any, is mailed by the ERCB to the licensee in response to the licensee's request for that document.

The conditions for certification are basically the same as those existing under the Exploratory Drilling Incentive System with one major simplification. While maintaining the distance requirement from a pre-existing productive well at 4.8 kilometres and the producing zone depth difference at 150 metres, it is now necessary for the ERCB to determine only whether or not a pre-existing productive well is or was capable of producing crude oil or natural gas.

If the ERCB denies a certificate, the operator has 30 days to request a review by the ERCB. Additional information as described in ERCB Informational Letter IL 85-11 must be submitted to justify a review.

Spudding or deepening of a well must begin within 30 days of the certificate date or else it lapses. Although not required to do so, the ERCB attempts to notify a licensee when a certificate lapses. Whether or not the licensee has been notified by the ERCB, reapplication must be made for certification. The department will rely solely on the decision of the ERCB with respect to the validity of any certificate.

Off Target Wells

Under the Oil and Gas Conservation Regulations (A.R. 151/71) the ERCB has the authority to designate a well as being "off target". A well that is designated as being off target and on which a penalty is levied is not eligible for the Exploratory Gas Well Incentive Program.
The licensee may file an application with the ERCB for a spacing unit or target area change.
If the application is approved and the well is no longer considered off target, the well may be fully eligible for the benefits under this program, subject to all other eligibility requirements.
Any such benefits will be received from the month in which the application to the ERCB is

approved, a royalty holiday application is received by the department, or production started, whichever is latest.

It is the responsibility of the licensee to inform the department as to the lifting of the off target designation. The department will recognize the ruling of the ERCB as final in all situations relating to off target wells.

Freehold

The Exploratory Gas Well Incentive Program applies only in situations where there is a Crown interest in production and is limited to the extent of that interest. Hence, wells on wholly freehold property are not eligible for any benefit under this program.

Prior Benefits

It is the intention of the department to prohibit a well from receiving benefits under more than one incentive program. Accordingly, a well that has already received a royalty exemption as an incentive exploratory well under the Exploratory Drilling Incentive System (EDIS) (A.R. 378/72) or any subsequent EDIS regulation, or a well receiving a benefit under the Deep Gas Royalty Holiday Program will only be eligible for any benefits under this program in respect of a new qualifying interval.

Qualifying Interval

New Well

One of the benefit criteria under this program is depth related. The term "qualifying interval" has been developed to cover the drilled well depth that is used to determine benefits. A new exploratory gas well located more than 4.8 kilometres from a pre-existing productive well will have a qualifying interval equal to its total depth or the drilled depth to the base of the natural gas bearing interval of the deepest zone from which natural gas is being produced in paying quantities, whichever is shallower (Figure 6).

In all cases a pre-existing productive well in a crude oil or natural gas bearing interval is one that is currently producing, or has had the capability to do so as determined by the ERCB at some point subsequent to December 31, 1979.

In the case of a new well which is located less than 4.8 kilometres from a pre-existing productive well and for which the top of the natural gas bearing interval is at least 150 metres below the base of the deepest crude oil or natural gas bearing interval of a pre-existing productive well within a 4.8-kilometre radius, the qualifying

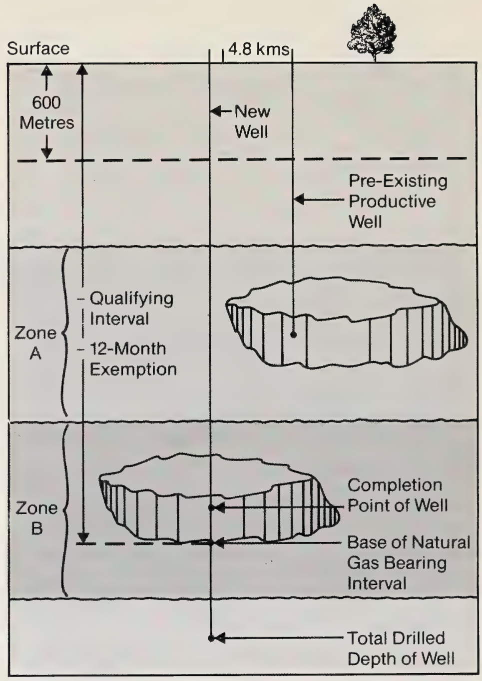


Figure 6 - Qualifying interval for a new well located more than 4.8 kilometres from a pre-existing productive well where the total drilled depth is beyond the base of the natural gas bearing interval.

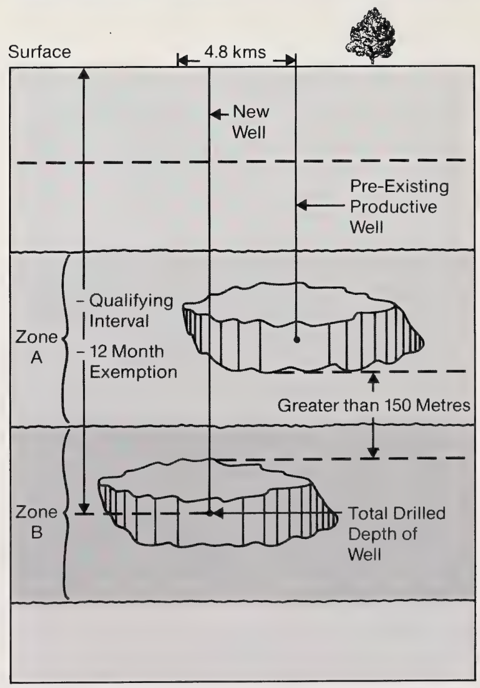


Figure 7 - Qualifying interval for a new well located within 4.8 kilometres of a pre-existing productive well where the completion point is at the total drilled depth. Royalty holiday applies to production from Zone B only.

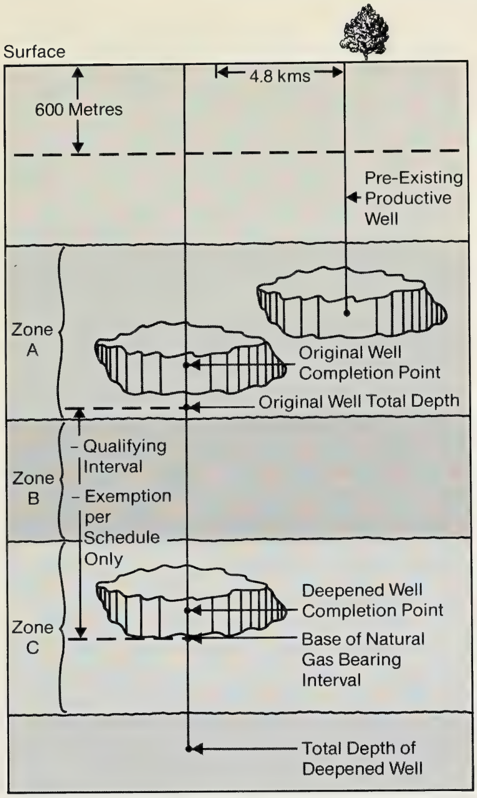


Figure 8 - Qualifying interval for a deepened well located more than 4.8 kilometres from a pre-existing productive well where the original well and deepened well total depths are beyond the bases of the natural gas bearing intervals.

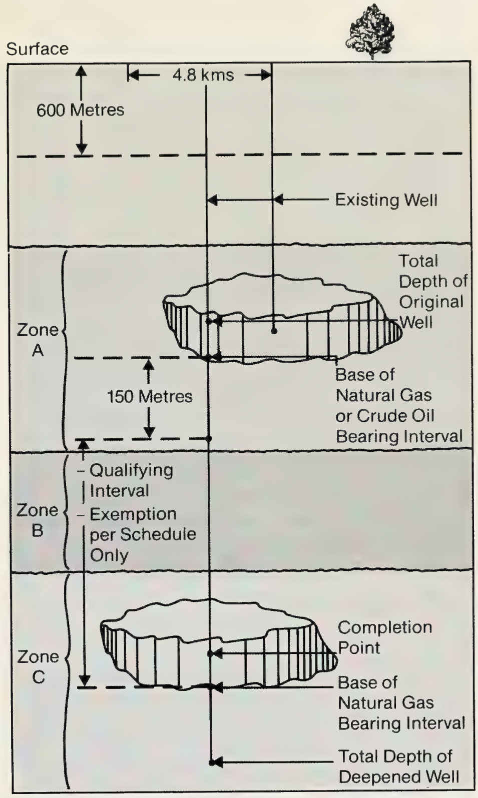


Figure 9 - Qualifying interval for a deepened well within 4.8 kilometres of a pre-existing productive well where the natural gas bearing interval is in a zone that is greater than 150 metres below the base of the natural gas bearing interval in which the pre-existing productive well is completed.

interval is equal to the total depth of the well, or the drilled depth to the base of the natural gas bearing interval of the deepest zone from which natural gas is being produced in paying quantities, whichever is shallower (Figure 7). Any well subsequently drilled to and completed in the same zone must be more than 4.8 kilometres from any pre-existing productive well in that same zone.

The department, as a general rule, will assume that when an owner begins to sell production, then the well is producing in paying quantities. In cases of doubt the department may conduct a specific review and make a final determination.

Deepened Well

Where a well located more than 4.8 kilometres from a pre-existing productive well is deepened, the qualifying interval is measured from the well's previous total depth to the deepened well's total depth, or from the base of the natural gas bearing interval of the deepest zone from which natural gas is being produced in paying quantities, whichever is shallower (Figure 8).

In the case of a deepened well which is located less than 4.8 kilometres from a pre-existing productive well, the qualifying interval is measured from 150 metres below the base of the deepest crude oil or natural gas bearing interval of a pre-existing productive well within a 4.8-kilometre radius, or the total drilled depth of the original well, whichever is deeper, to the total drilled depth of the well, or the drilled depth to the base of the natural gas bearing interval of the deepest zone from which natural gas is being produced in paying quantities, whichever is shallower (Figure 9).

As with a new well, the department will apply the same general rule for determining that there is production in paying quantities.

Benefits

Application Procedure

Application must be made on the Exploratory Gas Well Incentive Program Application (Form No. 548) and sent directly to the Incentives Branch of the Mineral Revenues Division. Application forms can be obtained directly from the Mineral Revenues Division or from the

locations noted on page ii. Incorrect applications will be returned. In these cases there may be a delay in the receipt of the benefits. This is particularly relevant where production has begun before a complete application is submitted. If an incomplete application is subsequently resubmitted and approved, then the date of the initial submission will be considered the effective month for the purpose of determining when the royalty holiday commences.

Applications must be received within six months of the finished drilling date for the well and must be accompanied by a copy of the certificate of the ERCB for the exploratory gas well. This is essential as the ERCB will no longer provide the department with a copy of each certificate as has been the practice under EDIS. In addition, the legislation requires that the drilling or deepening of the well be conducted diligently and continuously.

Delays caused by actions of a government department or agency may extend the time available for spudding or commencement of deepening.

Effective Date

The royalty holiday begins either on the first day of the month in which production begins or an application is received, whichever is later. This permits licensees to select the month of commencement of the royalty holiday. As desired, applications may be filed in order to exclude the month(s) in which test production occurs and/or to start the royalty holiday in the first month in which full production is expected.

Benefit Amount

The aggregate Crown royalty share value of natural gas and products to be exempted for a particular well is determined from the chart shown as Appendix 2 (Schedule 5 to the Natural Gas Royalty Amendment Regulation, A.R. 217/85). To calculate the benefit amount for a well in a specific area, when the qualifying interval is measured from surface the cumulative value at the deepest drilled depth not exceeding the depth drilled is added to the incremental value at that point times the number of metres in excess of that depth.

When the qualifying interval is not measured from the surface, i.e. it is in a deepened well, the benefit amount at both the beginning and finishing points of the qualifying interval must be computed in each case as if a well had been drilled from surface to each of those points. The difference between the two amounts so determined is the benefit for the deepened well.

The regulation stipulates that the well licensee is the party entitled to apply for the benefits under this program. Benefits may only be received by way of an offset against royalties that are payable on the well's production. As necessary, licensees may designate an agent, e.g. an operator, for the purposes of administering their interests under this program. It is not necessary to advise the department as to any agency arrangement.

It is the responsibility of well interest owners to obtain amendments to operating agreements, as required, to ensure receipt of an appropriate share of the benefits.

Limitations on Benefits

The royalty holiday for new wells will last until the value of natural gas and products exempted equals the amount determined from the chart shown as Appendix 2, or until 12 calendar months (not necessarily consecutive) of royalty-free production have occurred, whichever is later.

Regardless of which of the two limitations is applicable, the value of the royalty holiday cannot exceed $2 million per well.

In the case of deepening there is no 12-month time period exemption. The benefit computed from Appendix 2 will be received, subject only to the $2 million limit.

Benefit entitlements earned under this program must be used on or before May 31, 1998. Also, any unused benefits at the time of a well abandonment are lost. Production should be planned accordingly as the department does not have any discretionary authority to vary these conditions.

Inventories

Sometimes natural gas and products are not sold in the month of production. Consequently, product inventories can be carried for some time after the month of production. The department will record production months for the purposes of the 12-month limitation.

Crown/Freehold

Many production entities are split between the Crown and Freehold interests. In these situations, it is the intent of the program to provide a benefit with respect to the Crown's interest in production only. Accordingly, once the benefit is determined as if it were a 100% Crown well, it must be reduced to the level of the Crown interest. This also applies to the overall limitation of $2 million per well; i.e. the cap is reduced to $2 million times the Crown interest in the production entity. The 12-month time period exemption remains unaffected.

The Crown interest in production will be as of the date of application or first production, whichever is later, and will be on the basis of the

Crown/Freehold production split of the production entity in the month preceding the first month in which the royalty holiday applies.

Once the maximum level of the benefit to a Crown/Freehold well has been set, it will not be varied regardless of any subsequent changes in the Crown interest in the production entity. As the benefit can only be received by way of an offset against royalties that are payable, where the Crown's interest falls to zero per cent the unexpired benefit would become unusable and would be effectively lost, unless a restructured production entity restores a Crown interest to the well prior to May 31, 1998.

Twin Wells

The department recognizes that in certain circumstances a well may be inadvertently damaged, resulting in the need to drill a twin well. The department will rely on the recommendation of the ERCB as to the necessity for the well.

The unexpired benefits of the royalty holiday at the time the originally approved well was damaged and ceased production may be transferred to the twin well. To be eligible the twin well must be:

a) spudded after July 31, 1985;
b) located in the same DSU or legal subdivision, whichever is of lesser area, as the well being twinned; and,
c) capable of producing natural gas which, in the opinion of the ERCB, is not recoverable from the original well due to its inadvertent damage.

It is the responsibility of the licensee to advise the department of the new well identifier at the earliest opportunity. No increase or extension of a royalty holiday benefit will be gained by the drilling of a twin well.

Drilling Areas

The level of benefits available varies depending upon the area of the province in which drilling occurs. For this purpose, the province has been divided into four areas: the Northern, Foothills, Plains and Central areas. Benefits under the Northern and Foothills areas are the same. Each area is specifically defined by reference to township and range in Schedule 7 to the Natural Gas Royalty Amendment Regulation (A.R. 217/85).

Applicants should confirm the location of their well and hence benefit eligibility before applying. In the event of a disagreement on benefit entitlement due to location, the areas as defined in Schedule 7 (A.R. 217/85) will be used by the department to reach a final decision.

Appeals

An applicant may appeal each denied application in writing to the Associate Deputy Minister within 90 days of the date of the notice of the decision. Additional information must be presented in the appeal statement to justify a review of the department's decision.

The department will expeditiously review the appeal and advise the applicant as to the result. If the appeal is granted and the application approved, the benefit will be applied from the month in which the original application was made or the month in which production commenced, whichever is later.

Exploratory Drilling Incentive System (EDIS)

The Exploratory Drilling Incentive System ended July 31, 1985. The previously published eligibility requirements and administrative guidelines remained in effect until that date. In cases where an operator, due to the actions of a government department or agency, has incurred a delay such that the deadline cannot be met, the department should be informed of the circumstances upon application. Reasonable requests for extensions will be considered.

During the transition period, i.e. June 1 - July 31, 1985, the operator of an eligible well may obtain benefits under EDIS or, if necessary by agreement with the licensee, under the new Exploratory Gas Well Incentive Program or the Deep Gas Royalty Holiday Program. It is the sole responsibility of the operator and licensee to decide which benefit is desired and apply accordingly. The department does not have the authority to permit switching between programs.

Certain EDIS benefits, in the form of credits to the account of the beneficiary or a royalty exemption, may have been earned as of July 31, 1985. It is the intent of the department to provide a reasonable time for the use of these benefits. To meet this objective, a period ending December 31, 1990 is being allowed to make use of all earned benefits. Any unused amount outstanding at that date will be lost. Owners of the benefits are urged to plan their affairs to meet this date as the enabling legislation does not give the department any discretionary authority with respect to extension of the deadline.

DEEP GAS ROYALTY HOLIDAY PROGRAM

Eligibility

Requirements

To be eligible the spudding of the well or the commencement of drilling to deepen an existing well must start after May 31, 1985. As yet no closing date has been set for this program.

The drilling spacing unit (DSU) applicable to the zone in which the new or deepened well is completed must be wholly outside the deep gas pools, as defined by the ERCB, in effect on June 1, 1985. In addition, the depth of the producing interval in the well must be greater than 2 500 metres.

Exploratory Gas Well Incentive Program

A well may qualify for either the Exploratory Gas Well Incentive Program or this program, but not both. It is the responsibility of the licensee to select the program desired and apply accordingly.

Off Target Wells

Under the Oil and Gas Conservation Regulations (A.R. 151/71) the ERCB has the authority to designate a well as being "off target". A well that is designated as being off target and on which a penalty is levied is not eligible for the Deep Gas Royalty Holiday Program. The licensee may file an application with the ERCB for a spacing unit or target area change. If the application is approved and the well is no longer considered off target, the well may be fully eligible for the benefits under this program, subject to all other eligibility requirements. Any such benefits will be received from the month in which the application to the ERCB is approved, a royalty holiday application is received by the department, or production started, whichever is latest.

It is the responsibility of the licensee to inform the department as to the lifting of the off target designation. The department will recognize the ruling of the ERCB as final in all situations relating to off target wells.

Freehold

The Deep Gas Royalty Holiday Program applies only in situations where there is a Crown interest in production and is limited to the extent of that interest. Hence, wells on wholly freehold property are not eligible for any benefit under this program.

Prior Benefits

It is the intention of the department to prohibit a well from receiving benefits under more than one incentive program. Accordingly, a well that has already received a royalty exemption as an incentive exploratory well under the Exploratory Drilling Incentive System (EDIS) (A.R. 378/72) or any subsequent EDIS regulation, or a well receiving a benefit under the Exploratory Gas Well Incentive Program will only be eligible for any benefits under this program in respect of a new qualifying interval.

DSU Limitation

In cases where a well in the DSU applicable to the zone in which the new or deepened well has been completed has at any time received a royalty exemption under EDIS (A.R. 378/72) or any subsequent EDIS regulation, the Exploratory Gas Well Incentive Program, or this program, then no new well drilled or deepened in the same DSU can be eligible for this Deep Gas Royalty Holiday.

Licensees should note that a well in a DSU and which has been the beneficiary of drilling credits, but not a royalty exemption, does not disqualify another well in the same DSU from receiving benefits under this program.

Qualifying Interval And Pool

New Well

The benefit entitlement under this program is depth related. The term "qualifying interval" has been developed to cover the drilled well depth that is used to determine the benefit. In the case of a newly drilled well, the qualifying interval is the distance from a depth of 2 500 metres to the well's total depth (Figure 10) or to the base of the natural gas bearing interval of the deepest zone from which the well is producing natural gas in paying quantities (Figure 11), whichever is shallower.

Deepened Well

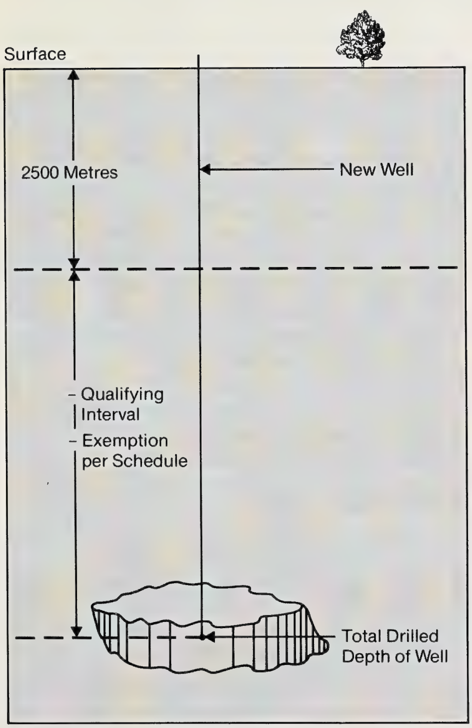
For deepened wells, the qualifying interval is the distance from the deeper of the 2 500-metre point or the previous total depth of the well to the deepened well's total depth (Figure 12) or to the base of the deepest natural gas bearing interval of the deepest zone from which the well is producing natural gas in paying quantities (Figure 13), whichever is shallower.

The department, as a general rule, will assume that when an owner begins to sell production, then the well is producing in paying quantities. In cases of doubt the department may conduct a specific review and make a final determination.

Qualifying Pool

A qualifying pool with respect to an eligible well is a natural gas occurrence that is not part of a deep gas pool as defined by the ERCB, in effect at June 1, 1985, and the top of which is at least at a depth of 2 500 metres. Cases where the pool straddles the 2 500-metre point will be reviewed on an individual basis by the department and will generally qualify if production in paying quantities initially occurs in the portion of the pool that is below 2 500 metres.

Figure 10 - New well qualifying interval where the completion point is at the total drilled depth of the well.



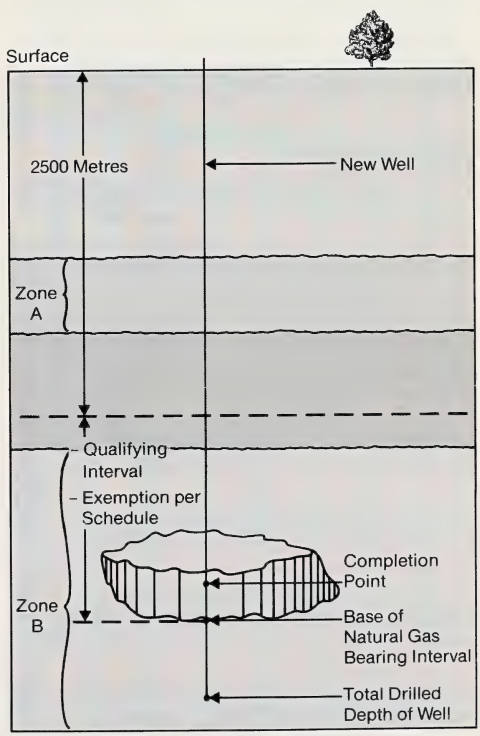


Figure 11 - New well qualifying interval where the total drilled depth of the well is beyond the base of the natural gas bearing interval.

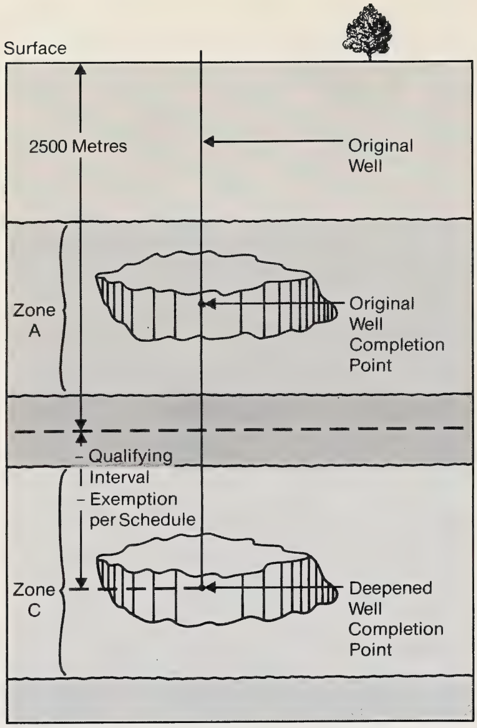


Figure 12 - Deepened well qualifying interval where the well is deepened from a completion point within a natural gas bearing interval above 2 500 metres. The royalty holiday applies to natural gas obtained from Zone C only.

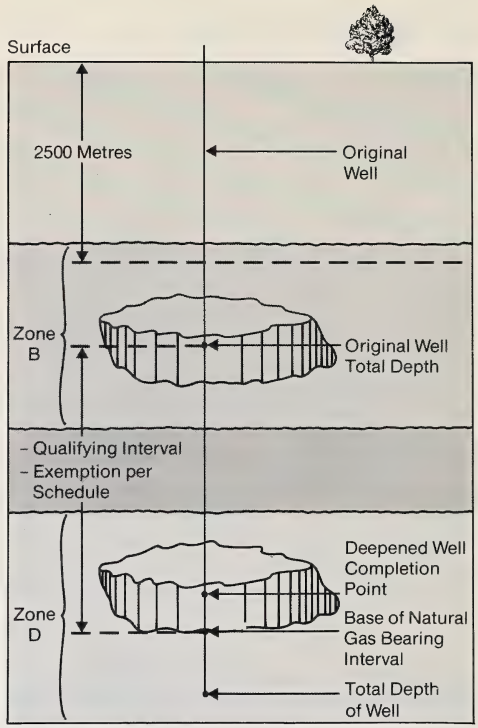


Figure 13 - Deepened well qualifying interval where the well is deepened from a completion point within a natural gas bearing interval below 2 500 metres. The royalty applies to natural gas obtained from Zone D only.

Benefits

Application Procedure

Application must be made on the Deep Gas Royalty Holiday Program Application (Form No. 549) and sent directly to the Incentives Branch of the Mineral Revenues Division. Application forms can be obtained directly from the Mineral Revenues Division or from the locations noted on page ii. Incorrect applications will be returned. In these cases there may be a delay in the receipt of the benefits. This is particularly relevant where production has begun before a complete application is submitted. If an incomplete application is subsequently resubmitted and approved, then the date of the initial submission will be considered the effective month for the purpose of determining when the royalty holiday commences.

Applications must be received within six months of the finished drilling date for the well. In addition, the legislation requires that the drilling or deepening of the well be conducted diligently and continuously.

Delays caused by actions of a government department or agency may extend the time available for spudding or commencement of deepening.

Effective Date

The royalty holiday begins either on the first day of the month in which production begins or an application is received, whichever is later. This permits licensees to select the month of commencement of the royalty holiday. As desired, applications may be filed in order to exclude the month(s) in which test production occurs and/or to start the royalty holiday in the first month in which full production is expected.

Benefit Amount

The aggregate Crown royalty share value of natural gas and products to be exempted for a particular well is determined from the chart shown as Appendix 3 (Schedule 6 to the Natural Gas Royalty Amendment Regulation, A.R. 217/85). To calculate the benefit amount, the cumulative value at the deepest drilled depth not exceeding the depth drilled is added to the incremental value at that point times the number of metres in excess of that depth. Appendix 3 applies to all regions of the province; hence location by region is not a factor in determining the benefit amount.

The regulation stipulates that the well licensee is the party entitled to apply for the benefits under this program. Benefits may only be received by way of an offset against royalties that are payable on the well's production.
As necessary, licensees may designate an agent, e.g. an operator, for the purposes of administering their interests under this program. It is not necessary to advise the department as to any agency arrangement.

It is the responsibility of well interest owners to obtain amendments to operating agreements, as required, to ensure receipt of an appropriate share of the benefits.The department will not and does not have the authority to settle benefits with any party other than the licensee or the agent of the licensee.

Limitations on Benefits

The royalty holiday will last until the value of natural gas and products exempted equals the amount determined from the chart shown as Appendix 3. Benefit entitlements earned under this program must be used within 10 years after the finished drilling date applicable to the drilled or deepened well. Any unused benefits at the time of a well's abandonment are lost.

Crown/Freehold

Many production entities are split between the Crown and Freehold interests. In these situations, it is the intent of the program to provide a benefit with respect to the Crown's interest in production only. Accordingly, once the benefit is determined as if it were a 100% Crown well, it must be reduced to the level of the Crown interest.

The Crown interest in production will be as of the date of application or first production, whichever is later, and will be on the basis of the Crown/Freehold production split of the production entity in the month preceding the first month in which the royalty holiday applies.

Once the maximum level of the benefit to a Crown/Freehold well has been set, it will not be varied regardless of any subsequent changes in the Crown interest in the production entity.
As the benefit can only be received by way of an offset against royalties that are payable, where the Crown's interest falls to zero per cent the unexpired benefit would become unusable and would be effectively lost, unless a restructured production entity restores a Crown interest to the well within 10 years of its finished drilling date.

Twin Wells

The department recognizes that in certain circumstances a well may be inadvertently damaged, resulting in the need to drill a twin well. The department will rely on the recommendation of the ERCB as to the necessity for the well.

The unexpired benefits of the royalty holiday at the time the originally approved well was damaged and ceased production may be transferred to the twin well. To be eligible the twin well must be:

a) spudded after May 31, 1985;
b) located in the same DSU or legal subdivision, whichever is of lesser area, as the well being twinned; and,
c) capable of producing natural gas which, in the opinion of the ERCB, is not recoverable from the original well due to its inadvertent damage.

It is the responsibility of the licensee to advise the department of the new well identifier at the earliest opportunity. No increase or extension of a royalty holiday benefit will be gained by the drilling of a twin well.

Special Case - Deepening

The department expects that a well which may previously have received a royalty holiday under either the Crude Oil Royalty Holiday Program, the Exploratory Gas Well Incentive Program or this program may be re-entered and completed in a deeper zone. In such cases section 2.20 of the Natural Gas Royalty Regulation (A.R. 16/74 as amended) permits the department to establish a qualifying interval. The well must meet all other eligibility requirements and the qualifying natural gas occurence must be either in a DSU that when the deepening commenced was completely outside any ERCB designated pool as at June 1, 1985 or above or below such a pool.

Any such entitlements must be used within 10 years of the finished drilling date of the well. Production should be scheduled accordingly as the department does not have the authority to vary this deadline.

Appeals

An applicant may appeal each denied application in writing to the Associate Deputy Minister within 90 days of the date of the notice of the decision. Additional information must be presented in the appeal statement to justify a review of the department's decision.

The department will expeditiously review the appeal and advise the applicant as to the result. If the appeal is granted and the application approved, the benefit will be applied from the month in which the original application was made or the month in which production commenced, whichever is later.

APPENDICES

Appendix 1

Volumes of Crown Royalty Share of Crude Oil Exempted Per Eligible Well

	Eligible Well Drilled in Northern Area or Foothills Area		Eligible Well Drilled in Central Area		Eligible Well Drilled in Plains Area	
Depth in Eligible Well to Base of Crude Oil Bearing Interval in Deepest Zone Producing in Paying Quantities (Qualifying Interval) (m)	Cumulative Volumes (m^3)	Incremental Volumes for Qualifying Interval (m^3/m)	Cumulative Volumes (m^3)	Incremental Volumes for Qualifying Interval (m^3/m)	Cumulative Volumes (m^3)	Incremental Volumes for Qualifying Interval (m^3/m)
0	0		0		0	
		0.6		0.3		0.2
500	300		150		100	
		0.6		0.3		0.2
1000	600		300		200	
		0.6		0.4		0.4
1500	900		500		400	
		0.9		0.5		0.4
2000	1350		750		600	
		0.9		0.9		0.5
2500	1800		1200		850	
		1.3		1.0		0.5
3000	2450		1700		1100	
		1.6		1.4		0.6
3500	3250		2400		1400	
		1.6		1.4		0.6
4000	4050		3100		1700	
		2.1		1.4		0.6

Appendix 2

Value of Crown Royalty Share of Natural Gas and Products Exempted Per Exploratory Gas Well

	Exploratory Gas Well Drilled in Northern Area or Foothills Area		Exploratory Gas Well Drilled in Central Area		Exploratory Gas Well Drilled in Plains Area	
Depth in Exploratory Gas Well to Base of Natural Gas Producing Interval in Deepest Zone Producing in Paying Quantities (Qualifying Interval) (m)	Cumulative Value ($000)	Incremental Value for Qualifying Interval ($/m)	Cumulative Value ($000)	Incremental Value for Qualifying Interval ($/m)	Cumulative Value ($000)	Incremental Value for Qualifying Interval ($/m)
0	0		0		0	
		120		60		60
500	60		30		30	
		140		80		60
1000	130		70		60	
		160		100		80
1500	210		120		100	
		180		120		100
2000	300		180		150	
		200		180		100
2500	400		270		200	
		320		300		100
3000	560		420		250	
		360		360		100
3500	740		600		300	
		380		360		100
4000	930		780		350	
		460		440		100
4500	1160		1000		400	
		480		520		100
5000	1400		1260		450	
		560		560		100
5500	1680		1540		500	

Appendix 3

Value of Crown Royalty Share of Natural Gas and Products Exempted Per Eligible Well

Depth in Eligible Well to base of Natural Gas Producing Interval in Deepest Zone Producing in Paying Quantities (m)	Cumulative Value ($000)	Incremental Value for Qualifying Interval ($/m)
2500	0	
		1000
3000	500	
		1000
3500	1000	
		1000
4000	1500	
		1300
4500	2150	
		1300
5000	2800	
		1600
5500	3600	